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SUBJECT: RAMADAN HIGHLIGHTS EGYPTIANS' INFLATION CONCERNS

REF: A. Cairo 0361
[B. Cairo 2588](#)
[C. Cairo 2887](#)
[D. Cairo 2983](#)

Sensitive but unclassified. Please handle accordingly.

Summary

[1](#)1. (SBU) Egypt's overall inflation rate declined over the summer from a peak of 12% year-on-year (y-o-y) in March 2007, but ticked up again with the start of Ramadan in September. Some of the increase is attributable to new Consumer Price Index (CPI) methodology introduced at the beginning of September. But most of the increase, particularly the 16.4% y-o-y increase in food prices, is due to the annual "Ramadan effect." Wholesalers and retailers take advantage of higher consumption and consumer expectation of higher costs to raise prices beyond reasonable profit margins. Hoarding of traditional food items exacerbates the problem, as does lack of an organized consumer sector. This year, the GOE responded with the usual rhetoric about stricter control of markets, but did not call for voluntary price restraints or issue price guidelines, as in past years. Global variables, such as record high international prices for wheat have led to higher bread prices and public protests. Both private observers and GOE officials, while concerned about public discontent, do not believe it will become unmanageable.

Inflation Trending Down, but Food Prices Jump during Ramadan

[1](#)2. (U) Egypt's inflation rate began to decline over the summer, after peaking at 12% y-o-y in March 2007. The rate decreased to 8% y-o-y in July, and remained relatively steady at 8.4% y-o-y in August. The decline bears out the Central Bank's claim that the steep rise in inflation in the early months of 2007 was pass-through from the 2006 Avian Influenza outbreak and fuel subsidy adjustments (Ref. A). But inflation ticked up again with the start of Ramadan on September 13. By the end of September, the monthly inflation rate had reached 10.5% y-o-y, and food prices had jumped dramatically, by 16.4% y-o-y.

[1](#)3. (U) Some of the up-tick can be attributed to a new CPI unveiled in early September. The new index, developed with assistance from the U.S. Bureau of Labor Statistic and the IMF, adds new items to the consumer basket, adjusts the weighting of items, including food, beverages and housing, and uses new methodology to calculate the inflation rate. The new index is based on a 2004/2005 Household Income and Expenditure Survey. Some analysts were surprise that

September's overall inflation rate (10.5%) did not increase more with introduction of the new CPI. The last time the GOE updated the CPI, in July 2004 (using a 1999/2000 Household Income and Expenditure Survey as the base year), inflation jumped from 4.4% in June 2004 to 17% in July 2004. The IMF projects inflation in the 6-9% range in the coming year, as Egypt's economic recovery continues and the GOE carries through with planned energy subsidy reductions.

The "Ramadan Effect"

¶4. (U) While the increase in overall inflation from August to September was less than some expected, the 16.4% y-o-y increase in food prices in September was right in line with predictions for Ramadan. Last year saw an 11.8% y-o-y increase in overall inflation and a 15.1% increase in food prices in October, the month in which most of Ramadan fell. Average food inflation was for all of 2006 was 10%. According to a study by the Institute of National Planning (INP), family expenditure on basic foodstuffs increases on average 30% during Ramadan, due to higher consumption (despite daily fasting) and higher food prices. The INP researchers noted that both wholesalers and retailers take advantage of higher consumption and consumer expectation of higher costs to increase prices beyond reasonable profit margins. Many suppliers and shopkeepers begin raising prices by up to 50% even before the start Ramadan.

¶5. (U) In addition to price gouging by wholesalers and retailers, local economists attribute some of the exaggerated price increases in Ramadan to lack of proper regulation of the food supply chain. Many wholesalers are not licensed, and engage in anti-competitive practices, such as hoarding supplies. Shopkeepers and even some individuals also hoard supplies, waiting for prices to increase before selling their stockpiles. In chronicling the annual Ramadan inflation, the media is full of reports of retailers blaming increases on suppliers, and vice versa. Neither sector is subject to consistent regulatory supervision, as Egypt lacks developed consumer protection mechanisms, and the nascent Egyptian Competition Authority (ECA) only investigates anti-competitive practices if a complaint is filed.

¶6. (U) Hany Kadry, Advisor to the Minister of Finance, told econoff that lack of an organized consumer sector is a major factor in price increases during Ramadan. Passive Egyptian consumers believe the government should control prices, and are unwilling to organize and make the annual price gouging unprofitable for the seller. Most consumers are unwilling to return even defective or spoiled items, as store-owners don't accept returns at all, even for defective/spoiled merchandise. Suppliers and retailers are also aware that consumers do not expect prices to decrease after Ramadan, so post-Ramadan prices remain at the higher levels reached during Ramadan. Kadry estimated that this "Ramadan effect" could go on indefinitely, until consumers are "no longer able to consume." But as long as the GOE provides a minimal annual public sector wage increase, most Egyptian families will be able to absorb the higher food prices through a combination of product substitution and "doing without," according to Kadry.

The Usual GOE Response

¶7. (U) This year, the GOE went through the usual motions in responding to Ramadan price increases, discussing the topic in Cabinet meetings, and calling for stricter control of markets, according to press reports. Even President Mubarak mentioned bringing inflation under control in his annual speech on October 6, the anniversary of the 1973 Yom Kippur War. Unlike in past years, however, the GOE did not call for voluntary price restraints or issue price guidelines, as this has proved completely ineffective in the past. Though the GOE has provided no substantive policy statements of how markets should be regulated, the government did set up some public markets/distribution points selling basic goods at pre-Ramadan prices. These distribution centers are not particularly well targeted, however, so middle income consumers can benefit as well as the poor.

International Factors Affecting Egypt

¶18. (U) In the months leading up to Ramadan, increases in international commodity prices, including wheat, corn and edible oils, also began affecting the prices of staple items in Egypt, bread in particular. In August, bread prices rose by 42%. The GOE allocated an additional LE 4.7 billion (\$836 million) for bread subsidies (the original allocation in the FY 2006/07 was LE 7.3 billion or \$1.2 billion) in response to the shortage, and has indicated it may allocate even more. The GOE did nothing, however, to alter the method of subsidization. Subsidized flour is provided to bakeries, which often re-sell the flour at market prices, rather than making low-cost bread for the poor (Ref. B).

¶19. (U) The increase in bread prices is reaching a crisis point in some areas of Egypt. Some analysts believe the crisis exacerbated recent protests by textile workers at one of Egypt's largest state-owned factories in the Nile Delta city of Mehalla El Kubra (Ref. C). Press reports indicated that many protesting textile workers were holding grocery store receipts to demonstrate the difficulties brought on by low/unpaid wages. The protesters succeeded in obtaining a 7% wage increase, which may lead to other strikes by workers from publicly-owned enterprises demanding wage increases in line with inflation rates (Ref. D).

Private and Government Observers Concerned, Somewhat

¶10. (SBU) Naglaa Azzam, a professor of sociology at Cairo University, told econoff that this year's bout of Ramadan inflation has strained the GOE's already tense relationship with the Egyptian people. But public discontent and disconnection with the government is not likely to spill over into civil disturbances, according to Azzam. Instead, Azzam believes the public will bottle up its frustrations, as it always does. Her views were echoed by Ahmed Abulzeid, Assistant Minister of Investment, who told econoff that he believes that even with the new CPI index, inflation figures are still understated. But public discontent will not become a "revolution," as the GOE will, in the short run, meet the minimum demands of the public. He feared, however, that protests such as those in Mehalla El Kubra could become more violent, leading to more violent government crackdowns, as the GOE values domestic tranquility above all else.

Comment

¶11. (U) Although Egyptian consumers look to the government to control prices, the GOE appears less inclined than in the past to intervene in the market and impose even voluntary price controls. One of the long term benefits of economic growth is the appearance of new producers and retailers, whose additional competition in the marketplace should drive prices down. Unfortunately, Egypt's impressive economic growth rate has not yet brought about this result. For the foreseeable future, consuming, one of the major activities of Ramadan, will still be hard on the average Egyptian's pocketbook.

JONES